BEFORE THE
TENNESSEE STATE BOARD OF EQUALIZATION

In Re:	Clean Harbors, Inc. Personal Property Account No. 1027236 Tax years 2004, 2005, 2006	)))	Hamilton County

INITIAL DECISION AND ORDER

Statement of the Case

The subject property is presently valued for tax purposes as follows:

TAX YEAR	APPRAISAL	ASSESSMENT
2004	$840,913	$252,274
2005	$875,127	$262,538
2006	$906,106	$271,832

The taxpayer filed appeals with the State Board of Equalization ("State Board") on October 21, 2005 (relative to tax years 2004 and 2005) and July 19, 2006 (relative to tax year 2006).[1]

The undersigned administrative judge conducted a hearing of this matter on February 28, 2007 in Chattanooga.[2] The appellant, Clean Harbors Environmental Services, Inc. ("Clean Harbors"), was represented by Wayne R. Kramer, Esq., of Kramer Rayson, LLP (Knoxville). Hamilton County Property Assessor's representative John Campbell was assisted by Byron Ellis, of the contract auditing firm Tax Management Associates ("TMA").

Findings of Fact and Conclusions of Law

Background. Clean Harbors is a Delaware corporation which provides a variety of environmental services including hazardous waste management, treatment, and disposal. On February 22, 2002, Clean Harbors entered into an agreement to acquire the nationwide assets of the chemical services division of a similar company – Safety-Kleen Corporation ("Safety-Kleen") – that was involved in a bankruptcy proceeding. Exhibit 2. Among those assets was a facility at 3300 Cummings Road in Chattanooga, where the tangible personal property in

[1]The 2004 and 2005 appeals are direct appeals pursuant to Tenn. Code Ann. section 67-1-1005(b) from back assessments/reassessments in the amounts of $153,666 and $175,380, respectively. The values for tax year 2006 were determined by the Hamilton County Board of Equalization upon consideration of the taxpayer's complaint pursuant to Tenn. Code Ann. section 67-5-1407. By order of Administrative Judge Mark J. Minsky, these appeals were consolidated for hearing.

[2]The last document made part of the record in this case (a spreadsheet detailing the purchase price allocation discussed *infra*) was received on May 8, 2007.

question is located. This property is currently used (or held for use) by Clean Harbors in the disposal of controlled substances.

The closing of the Safety-Kleen/Clean Harbors transaction, which included certain intangibles and liabilities as well as real and personal property, occurred in September, 2002. In accordance with Section 1.8 of the Acquisition Agreement, the parties negotiated an allocation of the purchase price for tax purposes.

Steve Long, managing partner of the Texas-based firm (Industrial Valuation Services) which handles Clean Harbors' property tax matters, appeared as a witness for the appellant. Mr. Long, who has represented hazardous waste management companies for the past 15 years, testified that the purchase price allocation was predicated on an independent appraisal of the transferred assets by Standard & Poor's. Particularly since the passage of the Sarbanes-Oxley Act of 2002, he stressed, such an allocation must be based exclusively on fair market value considerations.

In each of the tax years under appeal, Industrial Valuation Services timely filed on Clean Harbors' behalf tangible personal property schedules for the above business location with the Hamilton County Property Assessor's office. Exhibit 1. Attached to each report was a detailed listing of the personal property acquired from Safety-Kleen, along with the value assigned to each item in the purchase price allocation and entered on the taxpayer's books.[3] Clean Harbors claimed that such property should be appraised at its purported "original cost" (i.e., the allocated value in 2002) less standard depreciation.

The Assessor originally accepted the taxpayer's reported values in tax years 2004 ($328,693) and 2005 ($290,527). However, following an audit of the subject account by TMA, he determined that "[t]he total cost of owned equipment was under reported in tax years 2004 and 2005 by $3,121,177 and $3,158,334, respectively." Exhibit 4. On that ground, the Assessor issued certifications of back assessment/reassessment (Exhibit 6); and Clean Harbors appealed to the State Board.

In tax year 2006, when Clean Harbors' back assessment/reassessment appeals were still pending, the Assessor made an "adjusted assessment" on the subject account in conformity with the audit finding. After unsuccessfully contesting that assessment before the Hamilton County Board of Equalization, Clean Harbors filed an appeal with the State Board for that tax year as well.

Contentions of the Parties. Mr. Ellis, who personally conducted the TMA audit, believed that Clean Harbors' renditions contained "unintentional misstatements" of the actual

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[3]Also reported on the tangible personal property schedules were items that Clean Harbors purchased from other vendors after September, 2002. The valuation of those items is not in dispute.

cost of the property in question. He cited several examples of what appeared to be unrealistically low "purchase price reallocation" values for office furniture and equipment. It was his and Mr. Campbell's position that, in the absence of "original invoice price" information, the cost figures previously reported on the *seller's* (Safety-Kleen's) tangible personal property schedules yielded more accurate estimates of value.

Characterizing this dispute as merely a difference of opinion as to value, Mr. Kramer denied that Clean Harbors was guilty of any "misstatement" or other act or omission that would authorize a reassessment of the subject property. In any event, he maintained that:

> ...[T]here could be no better evidence of the fair market value of the tangible personal property at issue...than the purchase price paid by Clean Harbors in an arm's-length transaction only a matter of months before the filing of its first Property Report. Clean Harbors did exactly what the law requires. It reported the fair market value of its tangible personal properties by reporting the cost of such property to it.

Pre-Hearing Brief, p. 12.

Applicable Law. Tenn. Code Ann. section 67-5-601(a) provides (in relevant part) that "[t]he value of all property shall be ascertained from the evidence of its sound, intrinsic and immediate value, for purposes of sale between a willing seller and a willing buyer without consideration of speculative values...."

Pursuant to Tenn. Code Ann. sections 67-5-901 et seq., the State Board has adopted a schedule for the self-reporting of tangible personal property. This schedule incorporates the statutory rates of allowable depreciation for the various categories of property listed in Tenn. Code Ann. section 67-5-903(f). State Board Rule 0600-5-.06(1) establishes a presumption that the fair market value of commercial and industrial tangible personal property other than raw materials, supplies, and scrap is "the original cost **to the taxpayer** less straight line depreciation, or the residual value, whichever is greater." [Emphasis added.] This presumption is rebuttable (by either the taxpayer or the assessor) upon the presentation of sufficient evidence to support a "non-standard" valuation. State Board Rule 0600-5-.07.

The taxpayer must return the tangible personal property schedule to the assessor by March 1 of each year. Tenn. Code Ann. section 67-5-903(b). The assessor is ordinarily required to complete the assessment of all taxable property within his or her jurisdiction not later than May 20 of each year. Tenn. Code Ann. section 67-5-504(b). However, subject to the provisions of Tenn. Code Ann. sections 67-1-1001 *et seq.*, an assessor may make a "reassessment" of property thereafter when such property has been assessed "at less than actual cash value by reason of any fraud, deception, misrepresentation, **misstatement**, or omission of full statements of the owner of the property or the owner's agent or attorney." Tenn. Code Ann. section 67-1-1002(a)(2). [Emphasis added.]

As the party seeking to change the current assessments of the subject property, Clean Harbors has the burden of proof in this administrative proceeding. State Board Rule 0600-1-.11(1).

Analysis. In Alcoa Inc. (Blount County, Tax Years 2001 and 2002, Initial Decision and Order, February 16, 2006), following an audit, the assessor reassessed certain industrial vehicles on the ground that they were incorrectly listed on the taxpayer's tangible personal property schedule under GROUP 9 (Vehicles). In response to Mr. Kramer's argument that those articles were immune from reassessment because they had been duly assessed as reported, the undersigned administrative judge held that:

> The purpose of an audit is not only to discover unreported property, but also "to determine if the taxpayer has reported properly." State Board Rule 0600-5-.05(2). Surely such a determination would entail review of the grouping of the assets listed on the schedule. After all, the standard rates of depreciation to be applied under Tenn. Code Ann. section 67-5-903(f) obviously depend on the grouping of those items.

Id. at p. 3.[4]

In the instant case, on the other hand, there is no dispute as to the proper grouping of tangible personal property assets. Rather, the primary issue is whether Clean Harbors "misstated" its original cost for the subject property.

Although the terms *historical cost* and *original cost* are sometimes used interchangeably, there is an important distinction between them in the realm of accounting. As explained in an authoritative textbook:

> *Historical cost* is the actual or first cost of a property at the time it was originally constructed and placed in service. It should not be confused with *original cost*, the latter term more properly being used to designate the **actual cost to the present owner**, who may have purchased the property at a price more or less than the historical or first cost. [Emphasis added.]

American Society of Appraisers, *Appraising Machinery and Equipment* (1989), p. 60.

But Clean Harbors, of course, did not buy the subject property separately. How should the taxpayer's original cost be determined in the event of a purchase of multiple assets or an entire business? The State Board's current rules concerning the assessment of commercial and industrial tangible personal property do not specifically address this problem.[5]

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[4]Both parties took exception to the initial order entered in the Alcoa case, which is still pending before the Assessment Appeals Commission.

[5]On January 23, 2006, the State Board held a hearing on proposed rulemaking amendments which, *inter alia*, would have clarified the definition of "original cost" in Rule 0600-5-.01 and required a buyer of used personal property to "provide proof that the price or allocated price claimed as the current owner's cost reasonably approximates the current value" of such property. To date, the State Board has taken no action on this proposal.

If Clean Harbors were seeking "nonstandard" values – i.e., values different from those derived by original cost less straight line depreciation (or residual values, if greater) – the company would probably have been sent packing. The amount for which a debtor's assets are liquidated in a bankruptcy proceeding is a dubious indicator of the *market value* of those assets. Further, Clean Harbors never introduced the third-party appraisal on which the purchase price allocation was supposedly based. The administrative judge knows of no instance where the State Board has accepted a purchase price allocation alone as sufficient documentation for a *nonstandard* value. *See*, e.g., American Water Heater Company (Washington County, Tax Year 2003, Final Decision and Order, September 28, 2004).

In the mind of the administrative judge, however, that is not the situation here. Consistent with the terms of State Board Rule 0600-5-.06, the instructions for completion of the Assessor's Tangible Personal Property Report directed the taxpayer to "[l]ist the total original cost **to you** for each group by year acquired." [Emphasis added.] Hence, as the new owner of the subject property, Clean Harbors justifiably entered the "purchase price reallocation" value as its actual cost for each item listed.

To be sure, the Assessor was not obliged to accept the values reported by the taxpayer. In tax years 2004 and 2005, the Assessor could have made an "adjusted assessment" of the subject property – as he eventually did in tax year 2006. Nevertheless, the presumption in favor of a standard valuation remains operative for all three tax years under appeal. No presumption of correctness attaches to the Assessor's value if it is predicated on information other than original cost *to the taxpayer*.

The administrative judge has previously observed that "it is of no avail to the proponent of a non-standard valuation of tangible personal property to calculate what the standard valuation of such property would likely have been in the hands of a predecessor." ICI Acrylics (Shelby County, Tax Year 1998, Initial Decision and Order, September 15, 2000), p. 3. That this principle applies to the assessor as well as the taxpayer was recently demonstrated in 6161 Shelby Oaks LLC (Shelby County, Tax Year 2005, Initial Decision and Order, February 2, 2007). There, the appealing taxpayer had purchased the real property, machinery, equipment, and inventory associated with a health club whose former operator had defaulted on a promissory note to the seller. On its tangible personal property schedule for the following tax year, the appellant reported the personal property at the amount allocated to it in the asset purchase agreement. But the assessor refused to accept the reported value, instead appraising the property on the basis of the historical "cost on file" figures printed on the schedule. The administrative judge held that the historical cost figures alone were insufficient to support the practical equivalent of a nonstandard value under State Board Rule 0600-6-.07.

TMA and the Assessor have essentially followed the same methodology here – albeit after an audit of the subject account. To be sure, it strains credulity to posit that some of the

items Clean Harbors purchased from Safety-Kleen (e.g., filing cabinets; desks; credenzas) were worth as little as the $1-$3 amounts allocated to them. From an appraisal standpoint, however, such anecdotal evidence does not satisfactorily establish that the subject property in the aggregate was undervalued as reported.

In the cost approach to valuation of real property, accrued depreciation is deducted from replacement or reproduction cost new. It is axiomatic among real estate appraisers that estimates of replacement or reproduction cost must be typical of the market. *See*, e.g., International Association of Assessing Officers, Property Appraisal and Assessment Administration (1990), p. 207. By contrast, for better or worse, the Tennessee General Assembly and State Board have elected to base the "standard" valuation of personal property in this state on the present owner's actual acquisition cost. Arguably, the benefit of the rebuttable presumption in favor of standard depreciated cost should not extend to a taxpayer who acquires tangible personal property in a forced sale or other non-arm's-length transaction. But that is a policy decision for the legislature and/or State Board.

In light of the above considerations, the administrative judge need not rule on the legal argument that the Assessor lacked the power to reassess the subject property under Tenn. Code Ann. sections 67-1-1001 *et seq.*[6]

Order

It is, therefore, ORDERED that the following values be adopted for the tax years in controversy:

TAX YEAR	APPRAISAL	ASSESSMENT
2004	$328,693	$98,608
2005	$290,527	$87,158
2006	$318,935	$95,680

Pursuant to the Uniform Administrative Procedures Act, Tenn. Code Ann. §§ 4-5-301—325, Tenn. Code Ann. § 67-5-1501, and the Rules of Contested Case Procedure of the State Board of Equalization, the parties are advised of the following remedies:

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[6]In 2005, the legislature amended Tenn. Code Ann. section 67-5-902 by adding the following new subsection:

> (b) If a taxpayer would be liable for additional tax due to back assessment of property omitted from a reporting schedule, **or due to reassessment of property included in the schedule**, the taxpayer may offset this liability by showing that other property listed on the schedule was over reported, or by providing information that the reassessed property or other property listed on the schedule should be valued using a nonstandard method that more closely approximates fair market value. [Emphasis added.]

Thus the present law explicitly contemplates the possible reassessment of property listed on the taxpayer's return.

1. A party may appeal this decision and order to the Assessment Appeals Commission pursuant to Tenn. Code Ann. § 67-5-1501 and Rule 0600-1-.12 of the Contested Case Procedures of the State Board of Equalization. Tennessee Code Annotated § 67-5-1501(c) provides that an appeal **"must be filed within thirty (30) days from the date the initial decision is sent."** Rule 0600-1-.12 of the Contested Case Procedures of the State Board of Equalization provides that the appeal be filed with the Executive Secretary of the State Board and that the appeal **"identify the allegedly erroneous finding(s) of fact and/or conclusion(s) of law in the initial order"**; or

2. A party may petition for reconsideration of this decision and order pursuant to Tenn. Code Ann. § 4-5-317 within fifteen (15) days of the entry of the order. The petition for reconsideration must state the specific grounds upon which relief is requested. The filing of a petition for reconsideration is not a prerequisite for seeking administrative or judicial review.

This order does not become final until an official certificate is issued by the Assessment Appeals Commission. Official certificates are normally issued seventy-five (75) days after the entry of the initial decision and order if no party has appealed.

ENTERED this 13th day of June, 2007.

Pete Loesch

PETE LOESCH
ADMINISTRATIVE JUDGE
TENNESSEE DEPARTMENT OF STATE
ADMINISTRATIVE PROCEDURES DIVISION

cc: Wayne R. Kramer, Attorney, Kramer Rayson, LLP
Bill Bennett, Hamilton County Assessor of Property

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